OXFORD ANALYTICA

INDONESIA

MONETARY TRANSPARENCY

Country Report 2005

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INDONESIA

COMPLIANCE RATINGS

Monetary transparency	*2005*	*2004*	*2003*	*2002*
Clarity of roles	●●●●	●●●	●●●	●●●
Open decision process	●●●●	●●●●	●●●●	●●●●
Availability of information	●●●●	●●●●	●●●	●●●
Central bank accountability	●●●	●●●	●●●	●●●
Score	**3.75**	**3.50**	**3.25**	**3.25**

OUTLOOK & COMMENTARY

In July 2005, the central bank -- Bank Indonesia (BI) -- implemented a new monetary policy framework consistent with the inflation-targeting scheme. The new framework has four fundamental elements: the use of the BI reference rate as an operational target; a forward-looking monetary policy decision process; a more transparent communication strategy; and enhanced policy coordination with the government. The new framework has also provided for the release of an advance meeting schedule for Board of Governors meetings and quarterly Monetary Policy Reports.

BI Law No. 3/2004 created the Bank Indonesia Supervisory Board (BISB), with its members appointed by the House of Representatives (DPR). By law, the role of the BISB -- yet to become fully operational -- is only related to the good governance of BI, and should have no input into monetary policy. Concerns about the potential challenge to BI's independence should be allayed once the BISB demonstrates its role in helping the DPR in conducting surveillance of BI's accountability, independence, transparency and credibility.

EXECUTIVE SUMMARY

3.75 Compliance in progress

Indonesia subscribes to the IMF Special Data Dissemination Standard (SDDS), and the country meets specifications for coverage, periodicity, and timeliness of data related to the analytical accounts of the central bank and the banking sector as a whole. Information on the analytical accounts of the central bank is provided on a weekly basis (four times per month), and no later than two weeks after the end of the reference week. Data on Indonesia's aggregate open market transactions can be found on BI's website.

In July 2005, Bank Indonesia (BI) implemented a new monetary policy framework consistent with the inflation-targeting scheme. The new framework has four fundamental elements: the use of a BI reference rate as an operational target; a forward looking monetary policy decision process; a more transparent communication strategy; and enhanced policy coordination with the government. The new framework has also provided for the release of an advance meeting schedule for Board of Governors meetings and quarterly Monetary Policy Reports.

Law No. 24/2004 establishing a deposit insurance agency -- the Indonesia Deposit Insurance Corporation -- became effective in September 2005. The blanket guarantee has been replaced by a regular deposit insurance scheme administered by the deposit insurance agency. In contrast to the previous emergency bank liquidity programme BLBI scheme, the lender of last resort facility is only made available to address systemic problems and on the basis of constructive ambiguity.

In the past, BI's independence has been a source of political conflict, especially amid the 1997-98 Asian financial crisis, over issues of accountability. Some legislators have argued that a supervisory board should be created to oversee the actions of BI officials and to prevent the corrupt practices that have tarnished BI's reputation. Critics worry that such a board, if not designed properly or if it becomes politicised, could threaten central bank independence. At the time of writing, the Bank Indonesia Supervisory Board (BISB) had yet to become fully operational, although three of its members have already been selected. The full board will consist of five members chosen by the House of Representatives (DPR) and appointed by the president for three-year tenures, serving a maximum of two terms. The State Audit Agency (BPK) will remain responsible for auditing the central bank financial statements, and presenting these audits annually to the DPR.

Indonesia's overall score has improved from 3.50 in 2004 to 3.75

1. CLARITY OF ROLES, RESPONSIBILITIES, AND OBJECTIVES OF CENTRAL BANKS

●●●● Compliance in progress

The objectives and institutional framework of monetary policy

Central bank objectives and responsibilities

The objectives of Indonesia's central bank -- Bank Indonesia (BI), a separate legal entity from the government -- are specified in the Central Bank Act (CBA, Law No. 23/1999) and amendments to the CBA as established by BI Law No. 3/2004. The sole function of BI under the 1999 law was to maintain domestic price stability. BI Law No. 3/2004 establishes that BI has three roles, namely: (1) price stability; (2) regulation and supervision of the banking industry until the new Financial Services Authority Institution (FSAI) is established, at the latest in 2010; and (3) lender of last resort (LOLR) facility.[1]

BI has implemented an inflation-targeting framework. BI Law No. 3/2004 specifies that the central bank will conduct monetary policy to achieve an inflation target as determined by the government in consultation with BI. The central bank can decide which policies to set in order to achieve the inflation target -- so both the central bank and the government have responsibility for inflation.

BI is also empowered by the CBA to prescribe and implement monetary policy, regulate and safeguard the adequate operation of the payments system, and exercise banking supervision functions.[2] The law authorises the use of several monetary policy instruments, including open-market operations and setting both the interest rates and the minimum reserve requirements.

Under the CBA, most of the BI's banking supervision responsibilities are set to be transferred to a new institution, the Financial Services Authority Institution (FSAI), along with those currently exercised by the Ministry of Finance (MoF) and the Capital Markets Supervisory Agency (Bapepam). This transfer was originally set to take place by the end of 2002, although the BI was expected to retain some broad regulatory powers. However, the deadline was missed and the legislation chartering the FSAI remains under debate among legislators, the government and BI. The board's seven commissioners -- six of whom will be appointed by the president and one by BI's governor -- would have the power to regulate and supervise financial institutions and to abrogate their licences when deemed appropriate.

It appears that the establishment of the FSAI is a far more difficult task than first envisaged in law. BI Law No. 3/2004 set a delayed, perhaps more realistic, deadline of 2010 for the establishment of the FSAI. The new institution will require significant funding from the government, and it remains uncertain what level of resources, and from which revenue sources, the government will allocate in the medium term. The result has been slow progress and the need for a long implementation timeline.[3]

Operational autonomy

The CBA establishes that BI is fully autonomous in formulating and implementing monetary policy. External actors are strictly prohibited from interfering with BI's implementation of its tasks. Moreover, BI has the duty to refuse or disregard any attempt at interference in any form by any party. In order to further assure its independence, the CBA confers on BI a special position within the civil structure of the Republic of Indonesia. In May 2003, BI Governor

Burhanuddin Abdullah was sworn into office for a term of office to run from 2003 to 2008. This was the first time since BI's independence that the House of Representatives (DPR) had elected the central bank governor, instead of being handpicked by the president.

In the past, BI's independence was a source of political conflict, especially amid the Asian financial crisis, over issues of accountability. Some legislators have argued that a supervisory board should be created to oversee the actions of BI officials and to prevent the corrupt practices that tarnished BI's reputation. Critics (including the BI governor) worry that such a board, if not designed properly or if it becomes politicised, could threaten central bank independence.[4]

At the time of writing, the Bank Indonesia Supervisory Board (BISB) had yet to become fully operational, although three of its members have already been selected. The full board will consist of five members chosen by the DPR and appointed by the president for three-year tenures, serving a maximum of two terms. The State Audit Agency (BPK) -- the 'high state' auditing institution, partially independent from the government -- will remain responsible for auditing BI, and presenting these audits bi-annually to the DPR. Some commentators have repeatedly stated their concern over the possibility of politicisation of the BISB.[5]

Institutional relationship between monetary and fiscal operations

When necessary, BI engages in consultative coordination with the government. Coordination between the central bank and government usually takes place in a cabinet session on economic, banking and financial issues related to the duties of the central bank. On such occasions, the government may request BI's opinion on a policy matter. In addition, BI can also provide input to the government regarding the state budget and other policies relating to its duties and responsibilities. Government officials may attend the BI Board of Governors meetings, but have no voting rights.[6]

Lending to government

As set out in Article 56 of the CBA, the central bank is barred from providing any credit to the government and is no longer involved in financing development programmes or any type of government-directed spending. Information on the amounts and terms of overdrafts to the government, and on deposits of the government with BI, is disclosed on the BI website (in English and Indonesian). The same information can be found in the *Indonesian Financial Statistics*, published monthly by BI and released on its website, and in the IMF's monthly International Financial Statistics (IFS).

Under the amendments to the CBA, BI is allowed to purchase short-term (no longer than one-year) SUN (government bonds) in the primary market with a view to controlling the monetary aggregates. The medium- and long-term SUN can only be purchased in the secondary markets. These provisions are intended to ensure that the budget deficit is not financed by the central bank, which would undermine the inflation-targeting framework'.[7]

Central bank involvement in the rest of the economy

BI is authorised by the CBA to hold equity in entities such as clearing agencies, rating agencies and bank deposit guarantee agencies only if it is deemed necessary for the implementation of its tasks. Approval from the DPR should first be sought for investment in other types of institution. BI currently holds equity in a number of financial institutions, including *PT Bahana Pembinaan Usaha Indonesia, PT Askrindo,* and *Indover Bank* in the Netherlands. By law, BI should have divested interests in these institutions during 2002, but this was not fulfilled. As a result, the law was changed in order to extend the obligation of BI to divest its commercial interests to December 2008. As per last year, BI has been unable to find suitable buyers; the offers from prospective buyers have been too low to be acceptable and, as a result, the assets still remain on BI's books.[8]

Central bank profit allocation

Under Article 62 of the CBA, 30% of central bank profits must be placed in the Special Purpose Reserves account, and the rest of the surplus must be accumulated as a General Reserve account such that the total amount of capital and the General Reserves reaches 10% of all monetary liabilities. The rest of the surplus is distributed to the government and is exempt from any income taxes.[9]

Information on central bank profits, contained in surplus and deficit reports, is prepared and distributed internally. This information is gradually being made publicly available on BI's website. The monthly *Indonesian Financial Statistics* bulletin publishes time series data on BI accounts. The *Bank Indonesia Financial Report* includes detailed information of BI revenues, expenses, assets, liabilities and equity holdings.[10]

Agency roles performed by the central bank on behalf of the government

BI's agency roles for the government are stipulated in the CBA. Chapters VIII and IX cover all the categories stipulated in the IMF code, including BI's role as account holder of the government, manager of foreign exchange and domestic debt, and adviser to the government on economic and financial policies.

All regulations regarding BI's role in debt management are disseminated via the Government Gazette. Legislation and regulations are publicly available in Bahasa Indonesia; the availability of legislation and regulations in English has improved markedly in the past two years.[11]

2. Open Process for Formulating and Reporting Monetary Policy Decisions

●●●● Compliance in progress

The framework, instruments, and targets of monetary policy

Framework and monetary targets

BI has focused on maintaining price stability with a floating foreign exchange rate system. Previously, the central bank used base money as its operational target and set monthly base money targets. In July 2005, BI implemented a new monetary policy framework consistent with the inflation-targeting scheme. The new framework has four fundamental elements: the use of a BI reference rate as an operational target; a forward-looking monetary policy decision process; a more transparent communication strategy; and enhanced policy coordination with the government. These efforts are aimed at enhancing the effectiveness of monetary policy and achieving price stability.[12]

Following coordination between the MoF and BI, in September 2004 the minister of finance issued Decree No. 339/KMK.011/2004 setting out inflation targets for 2005, 2006, and 2007 as follows: 6%, 5.5%, and 5% with a deviation of +1%, respectively. The establishment of the Inflation Control Team, whose members represent several related agencies, has consolidated this coordination further.

In an effort to provide clearer information to the financial system regarding the goals of, and changes in, BI's monetary policy and future money supply, the central bank now targets changes in the interest rate of its short-term debt certificates (SBI), rather than base money, through the BI reference rate. The central bank may also intervene in the foreign exchange markets to help absorb liquidity and minimise excessive exchange rate fluctuations.

In January 2005, BI eliminated its overnight rupiah placement facility for commercial banks, which had been established to allow Indonesian banks to place excess liquidity with the central bank. BI eliminated this facility in response to concerns that its initial purpose of absorbing excess temporary monetary liquidity in the financial markets was no longer necessary given the stabilisation of the Indonesian financial system. Indonesian banks are still allowed to place excess liquidity with BI in seven-day time deposits, known as Bank Indonesia Deposit facilities (FASBIs). However, owing to pressure on the rupiah, at the end of August 2005 BI reopened its overnight rupiah placement facility to absorb excess liquidity in the market.

Monetary instruments

The CBA authorises the central bank to set monetary targets by taking into account the determined inflation rate target, relying on instruments such as open market operations on the rupiah and foreign exchange money market, the setting of discount rates and the BI reference rate, the setting of the statutory reserve requirements, and/or regulation of credit or financing.[13]

BI's monetary instruments largely consist of fortnightly auctions of SBIs (usually with one month to three-month maturity), as well as currency sterilisation to absorb excess liquidity in the economy and reduce exchange rate volatility. Effective 15 September 2005, BI banned rupiah margin trading against all foreign currencies in an effort to help stabilise the exchange rate.[14]

Press releases are used to explain the main considerations underlying BI's monetary policy decisions. Additionally, when SBIs are auctioned every two weeks the news of the interest rate goes to financial press coverage systems and is disseminated to the markets.

The monetary policy-making body

Monetary board

The CBA specifies the structure, composition, and functions of the Board of Governors. The board is charged with the formulation and implementation of monetary policy and meets at least once a month. Criteria for the selection of board members, rules on the conduct of meetings, and rules for voting and decision-making are also stipulated in the said Act. According to BI Law No. 3/2004, the governor of central bank can, for the first time, be selected from candidates outside BI, and therefore no longer has to be a BI officer.

The BI Board of Governors consists of a governor, a senior deputy governor, and at least four or a maximum of seven deputy governors. The governor and the senior deputy governor are nominated and appointed by the president, with approval from the DPR. The deputy governors are nominated by the BI governor and appointed by the president, with prior approval of the DPR. Board members are appointed for five-year terms, and may be reappointed to the same position for no more than one subsequent term. The Board of Governors is fully responsible for implementing the tasks and authorities of Bank Indonesia.[15]

Advance meeting schedule

In 2005, BI published for the first time an advance meeting schedule for Board of Governors meetings.[16] As stipulated in Article 43 of the CBA as amended by Law No. 3/2004, BI is required to hold monthly Board of Governors' meetings no less than once each month in order to stipulate general policies in the monetary sector.

The Board of Governors traditionally convenes every Tuesday to assess the economic situation and policy objectives, as well as any developments in previous months. The monthly meetings are immediately followed by a press release on the same day as the meeting. The meetings in April, July and October also assess the corresponding previous quarter, while the meeting in January focuses on the previous fiscal year. The quarterly meetings are followed by the publication of a quarterly report and data. Summary minutes of the board's meetings are released on the same day, and are also disclosed in the BI's Monthly, Quarterly and Annual Reports. Full transcripts of the meetings are not released, and there are no plans to do so since the information provided is perceived as adequate.[17]

Public statements on monetary policy

Periodic publications

BI posts changes to the setting of monetary policy instruments on its press release webpage, its *Monthly Review on Economy, Monetary, and Banking*, and the *Bank Indonesia Annual Report.* BI discloses its monetary policy objectives and policy considerations to the public by publishing summary minutes of BI board meetings. In addition, the results of BI board meetings are also disseminated through press conferences and are included in supplementary and quarterly reports. All of this information is available on BI's website.

The new, quarterly *Monetary Policy Report*, prepared within the context of the need for increased transparency and accountability, is part of the inflation-targeting framework launched in July 2005.[18] It incorporates the content that publications such as the quarterly *Economic, Monetary and Banking Developments -- Future Policy Directions* reports included. The *Monetary Policy Report* examines current economic conditions, the exchange rate and inflation, monetary policy, and banking sector policies. Economic forecasts and indications of future policy directions are also set out. In its chapter on 'Monetary Developments', the *Bank Indonesia Annual Report* includes similar information without the prospective emphasis, as well as a summary of monetary developments from the previous year. In addition, periodic press statements are released on matters relating to monetary policy.

Public hearings

Under the supervisory function of the DPR, the central bank is required by law to submit a quarterly progress report on the implementation of its duties and responsibilities. BI officials have regular meetings with key policymakers (at least once every three months) to discuss BI's decisions and the direction of monetary policy. In particular, they meet regularly with the legislature's Commission IX (overseeing financial issues) and with the Coordinating Ministry of the Economy. Less regular discussions are held with the legislature, largely depending on the legislators' schedules.

Meetings with the legislature are usually conducted with one party at a time, and BI pays special attention to briefing the research divisions of the top five political parties.[19] Central bank officials also meet with journalists and academics to discuss BI's activities.

Regulations on data reporting by financial institutions to the central bank

The CBA establishes BI's right to request data, information and reports from financial institutions. A summary of banking regulation is included in the *Bank Indonesia Annual Report* as part of the appendices. The report usually has a special chapter on 'Banks and Other Financial Institutions', where policies and information on banking policies, commercial banks and other financial institutions are reported. BI's website publishes consolidated statements of the banking sector. Banks are normally required to publish their reports once a year, although 'problematic' banks may have this requirement waived by a decision of the central bank. BI also publishes data on the analytical accounts of the banking sector, which cover both BI and commercial banks' operations.

After BI issued 'Know Your Customers' regulations (No. 3/2001) in June 2001, requiring banks to report suspicious transactions, the Indonesian legislature passed anti-money laundering legislation in March 2002, which was later amended in 2003. The Anti-Money Laundering Law (No. 15/2002) outlines measures to control attempts to hide illegally amassed funds. The revisions to the law widened the definition of money laundering to include the laundering of proceeds from gambling, prostitution, tax, and environmental crimes. In addition, the types of entities subject to transaction-reporting obligations have been broadened to include entities providing services related to the financial sector, such as post office services, as well as those providing financial services. In March 2002, BI issued Regulation No. 4/2/PBI/2002 requiring non-financial institutions to report their foreign exchange transactions with offshore parties to the central bank. Foreign exchange flows by companies with total assets or an annual sales turnover of at least 100 billion rupiah will be subject to the regulation. The new requirements supplement data on foreign exchange flows already furnished by banks and non-bank financial institutions.

The Anti-Money Laundering Law also established the independent Center for Financial Transaction Analysis and Reporting (PPATK), which submit their findings to the Attorney General's Office (AGO) and the Corruption Eradication Commission (KPK). By law, the PPATK commission should remain free from political intervention, responsible only to the legislature, and vested with the authority to investigate finance companies and persons suspected of being involved in money laundering crimes. The PPATK has sound investigative skills, and it has made arrangements to cooperate on investigations with Bapepam, BI, certain directorates of the MoF, the national police and the AGO. As a result of these efforts, Indonesia was removed from the Financial Action Task Force's 'blacklist' of non-cooperative countries and territories on 11 February 2005.[20]

3. PUBLIC AVAILABILITY OF INFORMATION ON MONETARY POLICY

●●●● Compliance in progress

Release of central bank data

Indonesia subscribes to the IMF Special Data Dissemination Standard (SDDS), and the country meets specifications for coverage, periodicity, and timeliness of data related to the analytical accounts of the central bank and the banking sector as a whole. Information on the analytical accounts of the central bank is provided on a weekly basis (four times per month), and no later than two weeks after the end of the reference week.[21] Weekly released data on Indonesia's aggregate open market transactions can be found on BI's website, on the Monetary Indicators page. Moreover, BI publishes the monthly bulletin *Indonesian Financial Statistics*.

An advance release calendar -- giving one-quarter prior notice of the approximate release dates, and later a one-week prior notification of the precise release dates -- is disseminated on the IMF's Dissemination Standards Bulletin Board.[22] The advance release calendar is updated monthly.

Information on foreign exchange reserves is available on the BI website. The website also discloses its claims on deposit money banks, domestic credit to the public sector, domestic credit to the private sector, gross foreign assets, and gross foreign liabilities. BI's website also publishes information on reserve money, currency in circulation, commercial banks' demand deposits at BI, and non-bank private sector demand deposits. In 2005, BI made efforts to report data on mutual funds (Reksadana) that issue deposit-like liabilities that have hitherto been excluded from the scope of monetary statistics. In 2005, central bank staff started working with the MoF's Directorate General of Financial Institutions (the supervisory agency for non-bank financial institutions) to start data compilation on finance companies, which will be followed by insurance companies' data in 2006, and pensions funds and mutual funds in 2007.[23]

The central bank balance sheet

BI publishes data based on its accounting records on a weekly basis, and no later than two weeks after the end of the reference week. The data are released simultaneously to all interested parties through BI's website, and are subsequently published in the *Weekly Report* and in the monthly bulletin *Indonesian Financial Statistics*. In addition, the central bank publicly discloses its balance sheet as part of the annual financial statement. The annual statements for 1998 to 2004 are available on the website. BI also releases information on the central bank's monetary operations.

BI is required to submit its annual financial statement to the State Audit Agency (BPK) for auditing, the result of which is reported to the DPR. The audited balance sheet and surplus/deficit statement are announced to the public through the mass media.

Lender of last resort

Substantial lender of last resort operations were carried out at the onset of the 1997-98 Asian financial crisis. BI injected large amounts of liquidity support to keep banks from defaulting and to keep the country's payments system functioning. In order to restore confidence, by January 1999 the central bank had lent 151 trillion rupiah in emergency support to 48 banks, much of it without proper collateral and with little more than the bankers' personal promises of repayment. In February 1999, 144.5 trillion rupiah (equivalent to 14 billion US dollars) of that amount was replaced by government-issued promissory notes. The nature of these loans, made under BI's emergency bank liquidity programme (BLBI), created serious concerns over transparency that still haunt BI.

After almost five years, in July 2003, the DPR finally approved an agreement between the government and BI to settle the liabilities arising from the emergency loans. The resolution should place no additional financial burden on the state budget or on BI, where the outstanding BLBI loans are to be replaced by government securities with payment derived from the surplus of BI, after meeting criteria for BI's capital to monetary liabilities ratio.[24]

When the introduction of liquidity support was unable to stop the runs on banks, the government in January 1998 announced a blanket guarantee for depositors and creditors of all Indonesian-incorporated banks. The BLBI programme thus included a guarantee of the claims of non-depositor creditors, applied to both on-balance and off-balance sheet bank liabilities denominated in either foreign currency or rupiah. The government repeatedly extended the guarantee programme in order to reduce uncertainty and allow time for the government to begin an orderly restructuring of the banking sector. The Financial Safety Net (FSN) team, which consists of BI and the MoF, designed a policy framework for lender of last resort operations in 2004, which includes legal provisions, operational rules and technical guidelines.[25]

With regard to lender of last resort operations, Law No. 24/2004 establishing a deposit insurance agency -- the Indonesia Deposit Insurance Corporation -- became effective in September 2005. The blanket guarantee has been replaced by a regular deposit insurance scheme administered by the deposit insurance agency.[26] In addition, in contrast to the previous BLBI scheme, the lender of last resort facility is only made available to address systemic problems and on the basis of constructive ambiguity. This means that if there is a similar systemic crisis within the banking sector and liquidity support is necessary to prevent a loss of confidence in the sector, then there should be a much more in-depth examination of the banks receiving the support, and far stricter criteria applied to banks requesting such liquidity support.

The Indonesian Bank Restructuring Agency (IBRA) was established in 1998, in response to the Asian financial crisis as an autonomous agency under the purview of the MoF. Its two main functions were to supervise banks in need of restructuring and to manage the assets acquired by the government under the BLBI restructuring scheme. Upon the closure of IBRA at the end of its five-year mandate in February 2004, the government established PT Perusahaan Pengelola Aset (PPA), a state-owned asset management company, to hold and manage the remaining assets previously owned by IBRA and not subject to ownership claims.[27]

Public information services

According to the CBA, BI must disclose monetary information to the public.[28] Public information services are comprehensive and include such publications as BI's *Annual Report* and the *Financial Report*, quarterly publications on economic, monetary and banking developments, and monthly reviews on monetary policy. In 1998, BI established a Communications Bureau in the Office of the Governor to relay information to the press and other stakeholders.[29]

BI maintains public information services both through its own website and through the IMF's SDDS site. This includes timely access to a variety of publications, including the *Monetary Policy Reports*. Moreover, the *Monthly Review on the Economy, Monetary Policy, and Banking* provides information on the central bank base money, its liquidity credit and support, open market operations, and the country's foreign exchange assets. Interviews with senior officials and progress reports on banking and monetary policy are also posted on the site. While not all documents are available in English, BI's website has greatly improved and today is one of the most informative and best-maintained Indonesian government websites. Availability of information in English has continued to increase in 2005. At the same time, information on BI's website is now being updated on a regular basis.

BI's Investor Information and Enquiries (IIE) website is designed to provide complete and accurate information about economic, financial, and banking conditions in Indonesia, as well as investment rules, regulations, and other information relevant for supporting investment decisions in Indonesia.[30] The site is also intended to establish a communication channel with investors and to counter incorrect or negative information about the country's financial markets. Since 2002, the IIE website has grown and now offers a variety of documents on topics such as fiscal sustainability, financial sector restructuring, and banking regulation.

4. ACCOUNTABILITY AND ASSURANCES OF INTEGRITY BY THE CENTRAL BANK

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Accountability before a designated public authority

The CBA requires that BI must always adhere to principles of accountability and transparency in implementing its duties, authorities and budget. BI is committed to strengthening its internal management through good governance. Significantly, the MoF Decree No. 339/KMK.011/2004 establishes that whenever there is deviation between actual and the target range of inflation, senior officers of the government and BI must explain to the parliament the reasons for such a deviation, and the expected measures that may be pursued to steer inflation back into the target.

In accordance with the CBA, BI's Board of Governors must regularly appear before legislative committees to explain the conduct of monetary policy, its objectives, its performance in reaching those objectives, and other general issues involving the state of the economy. The board also liaises frequently with other governmental bodies, such as the president, the coordinating minister of the economy, the MoF, and the Ministries of Trade and Industry.

BI must submit its annual report -- the *Bank Indonesia Annual Report* -- examining its monetary policy for the previous year, and presenting policies and targets for the coming year to the legislature, the president, and media.[31] Quarterly and requested reports are also submitted to the legislature. BI's internal operations budget should now be approved by the DPR according to BI Law No. 3/2004.

Financial statement

Audited financial statement

BI's financial statements can be found in the *Bank Indonesia Financial Report*.[32] Financial statements are audited by the BPK in accordance with the Governance Auditing Standard (SAP) established by the BPK, which incorporates the Professional Public Accounting Standards (SPAP) of the Indonesian Institute of Accountants. However, there is no comment on how these standards relate to internationally accepted principles.

External and internal audit

The BPK audits and discloses its results to the public. The BPK is constitutionally independent from the government to conduct its activities, although it is not yet financially independent; proposed changes to the Audit Board Law No. 5/1973 and the State Audit Law No. 15/2004 should provide the BPK with full independence in the near term. Cases of abuse and misuse of resources are noted in the BPK reports, which are submitted to the AGO and the police for further action. Although the onus is on these latter institutions to pursue criminal investigations, some commentators noted that these have become much more effective since the formation of the Coordinating Team for Combating Corruption (Timtastipikor) in April 2005.[33]

BI is taking steps to strengthen its internal control and accounting procedures. The BPK's 2003 annual audit of BI administrative operations and financial statements -- the first since the BLBI scheme was set up -- was the first to be categorised as 'unqualified', and thus there was no need to forward recommendations to the AGO. In matters of accountability and budget, the BPK may conduct a special examination of BI at the request of the DPR if deemed necessary.[34]

Internal governance procedures are partially disclosed in the CBA; these are also regulated by internal regulations that are not publicly disclosed. The Internal Audit Directorate (DPI) audits all of BI's departments and agencies, as well as its representative offices abroad. These are performance as well as financial audits.

In the past, the BPK has acknowledged the need to continue strengthening BI's audit processes, but did not want to recruit an independent accounting firm to carry out this work.[35] As an effort to institutionalise additional accountability measures, BI Law No. 3/2004 created the Bank Indonesia Supervisory Board (BISB), with its members appointed by the DPR. Article 58 (a) stipulates that the role of the BISB -- yet to become fully operational -- is only related to the good governance of the central bank, and should have no input into monetary policy. Therefore, the main task of the Supervisory Board would be to assist the DPR in conducting its surveillance of BI's accountability, independence, transparency and credibility. This surveillance function covers the assessment of (i) the BI annual financial report; (ii) BI's operational and investment budget; and (iii) decision-making processes (internal, not policy) other than those concerned with monetary policy and BI's asset management. Some commentators suggested that, at present, there is still uncertainty over the remit of BISB oversight, and hence the board will not start operations until these ambiguities are clarified.[36]

Conduct of officials

The CBA prohibits members of the Board of Governors from having any direct or indirect interests in any enterprises, from holding any other position concurrently in other entities, except where their tasks require them to hold such a position, and from holding membership or a management position in a political party.[37] Article 71 specifies the penalties to be imposed should a BI official illegally disclose confidential information, while Article 72 authorises the Board of Governors to impose sanctions on employees who fail to perform their obligations.

The CBA establishes that employees of BI are appointed and removed by the Board of Governors. Article 45 provides legal protections for officials and staff in the conduct of their official duties. The governor, the senior deputy governor, and any other BI official cannot be punished for decisions taken or policies implemented in accordance with the tasks and authority as prescribed in the Act, as long as these policies are conducted in good faith.

In September 2004, former BI Governor Sabirin Syahril was cleared by the Supreme Court of all corruption charges.[38] This was noted in BI's financial statement. The BPK's own audit of the matter found that Sabirin was not involved, and instead identified other BI and IBRA officials as potential suspects. The authorities have been slow in acting on the BPK's findings. The matter of how to deal with convicted officials has not been resolved, and it has become less pressing with the replacement of Sabirin Syahril by Governor Burhanuddin Abdullah.[39] Although Governor Burhanuddin is a career central banker, he has never been implicated in allegations of corruption that have tainted many of his colleagues and predecessors. For example, a third former BI director was convicted in April 2003 by a district court for his involvement in the BLBI scheme.[40]

The results of the BPK's special audit on the possible violation of the criminal and the anti-corruption law, the prosecution and sentencing of BI officials, and the management of recipients involved in the wrongful issue and criminal misuse of the liquidity loans, have largely remained opaque.[41] The State Finance Law of 2003 has strengthened standards for the conduct of public servants. In particular, Article 35 of the law makes government officials personally responsible for state funds under their control. Under the law, officials will face jail terms for embezzlement and mismanagement, and they will be forced to personally reimburse the state for any misused or embezzled public money. The law makes all civil servants subject to equal punishment for the same fiscal crime, regardless of rank. Although the law does not provide for a clear enforcement mechanism, the implementing regulations and the State Treasury Law of 2003 have gradually addressed the issue of proper enforcement. The State Treasury Law provides officials at both central and local levels with detailed rules governing the use and administration of state funds, establishes penalties and sanctions for violations by state treasurers, and contains clear stipulations on the settlement of government financial losses caused by mismanagement or corruption.

INTERVIEWS

Representatives of *Oxford Analytica* interviewed the following individuals during a visit to Indonesia between 14 and 17 November 2005:

Central Bank of Indonesia

15 November 2005

Charles Joseph	Senior Economist	Economics Research and Monetary Policy Department

Ministry of Finance (MoF)

14 November 2005

Saro Edi		State Budget Planning Division
Kunta Wibawa		Tax Revenue Division
Tity Hernawati		Non-tax Revenue Division

17 November 2005

Hekinus Manao	Director	Accounting and Information - Treasury
	Committee Member	Government Accounting Standards Committee

ADDITIONAL INTERVIEWS

14 November 2005

Anwar Nasution	Director	State Audit Agency (BPK)
Dr Soekoyo		State Audit Agency (BPK)

14 November 2005

Rajiv Sondhi	Senior Financial Management Specialist	World Bank
James Sheppard	Public Sector Management Consultant	World Bank

15 November 2005

Yougesh Khatri	Resident Representative	IMF

16 November 2005

Dedi Haryadi	Director	Bandung Institute of Governance Studies

NOTES

[1] See Central Bank Act, Nr. 23/1999 at: www.bi.go.id/web/en/Tentang+BI/UU+BI/UU23-1999/ and Amendment to the CBA, Nr. 3/2004 at: www.bi.go.id/web/en/Tentang+BI/UU+BI/UU3-2004/
[2] Article 8, CBA.
[3] Interviews in Indonesia, 14-17 November 2005. A major concern of BI is that it must have a smooth data flow in order to be able to perform its financial-sector stability functions. For instance, since 2003 BI has been operating a Bureau of Financial System Stability. It is thus important that this bureau receives accurate and timely data on the stability of the banks if it is to ensure overall sector stability. In BI's opinion, this should mean that data goes directly to BI, and should not have to pass through the FSAI. In general, it is still unclear how these roles will be divided between the FSAI and BI.
[4] See "BI opposes plan to set up supervisory board", *The Jakarta Post*, 18 September 2003.
[5] Interviews in Indonesia, 4-6 October 2004 and 14-17 November 2005. See also: "BI opposes plan to set up supervisory board", *The Jakarta Post*, 18 September 2003. In 2003, BI Governor Burhanuddin Abdullah stated: "The intention of setting up the [Supervisory] Board is good, but what happens in Indonesia is that good intentions are usually transformed into something bad by particular vested interests". There is ongoing debate on whether BISB's powers and authority should be expanded.
[6] See Chapter VIII of the CBA.
[7] See *2003 Economic Report on Indonesia.*
[8] Interviews in Indonesia, 4-6 October 2004 and 14-17 November 2005.
[9] Article 62, CBA.
[10] See "Laporan Keuangan Tahunan Bank Indonesia" (in Bahasa Indonesia only) at: www.bi.go.id/web/id/Riset+Survey+Dan+Publikasi/Publikasi/
[11] Interviews in Indonesia, 14-17 November 2005.
[12] Interviews in Indonesia, 14-17 November 2005.
[13] Article 10, CBA.
[14] Interviews in Indonesia, 14-17 November 2005. Margin trading allows investors to put up only a fraction of the amount they wish to trade while using borrowed funds to leverage the operations.
[15] See www.bi.go.id/web/en/Tentang+BI/Profile+DG/
[16] See "Tentative Schedule of 2005 Monthly Board of Governors' Meetings (RDG)" at: www.bi.go.id/web/en/Pengumuman/Board+of+Governors+meeting+05.htm
[17] Interviews in Indonesia, 4-6 October 2004 and 14-17 November 2005.
[18] See "Monetary Policy Report" at: www.bi.go.id/web/en/Riset+Survey+Dan+Publikasi/Publikasi/
[19] Interviews with Bank Indonesia officials, Jakarta, 20 November 2002 and 4-6 October 2004.
[20] Interviews in Indonesia, 14-17 November 2005.
[21] Analytical accounts of the central bank, provided by Indonesia as a subscriber to SDDS at: http://dsbb.imf.org
[22] Dissemination Standards Bulletin Board at: http://dsbb.imf.org
[23] Interviews in Indonesia, 14-17 November 2005. See also: "Indonesia: Report on the Observance of Standards and Codes - Data Module, Response by the Authorities, and Detailed Assessments Using the Data Quality Assessment Framework", 28 July 2005, at: www.imf.org/external/pubs/ft/scr/2005/cr05255.pdf
[24] *2003 Economic Report on Indonesia,* p.73. The Government will issue a treasury bond with the value of 144.5 trillion rupiah (14 billion US dollars), and with interest of 0.1% per annum. This new Treasury bond is the substitute of existing Government Bonds Nos.1 and 3, which were issued as the government's shares in covering emergency loans extended. The payment of the Treasury bond is derived from the surplus of BI, which constitutes the share of the government and is paid only when the capital to monetary liabilities ratio has reached 10%. In the case that the capital to monetary liabilities ratio is less that 3%, the government shall set up a budget to pay a charge that will enable the ratio to reach 3%. Interviews, Indonesia, 4-6 October 2004.
[25] "Economic Policy Package Pre- and Post-IMF Program", Coordinating Ministry of Economic Affairs, p.II-5, available at www.ekon.go.id/berita/20030917/20030917_1.shtml
[26] Interviews in Indonesia, 14-17 November 2005. Under the new arrangements, the government guarantees all third party deposits, but no longer interbank claims, during the first six months after 22 September 2005 (the date the law became effective); third party deposits up to five billion rupiah only, during the next six-month period; third party deposits up to one billion rupiah only, during the next six-month period; and third party deposits up to 100 million rupiah thereafter.
[27] Interviews in Indonesia, 14-17 November 2005.

[28] Article 58, CBA.
[29] Interviews in Indonesia, 4-6 October 2004.
[30] See www.bi.go.id/web/id/Info+Penting/IIE/ or www.bi.go.id/web/en
[31] Following CBA provisions, Article 58.
[32] See the latest 2004 financial report (In Bahasa Indonesia only) at: www.bi.go.id/web/id/Riset+Survey+Dan+Publikasi/Publikasi/Laporan+Keuangan/lktbi+2004.htm At the time of writing, the 2004 English copy was not available.
[33] Interviews in Indonesia, 14-17 November 2005. Timtastipikor pools the resources of the BPK, the police, the AGO, the Center for Financial Transaction Analysis and Reporting (PPATK) and others to investigate criminal activities.
[34] Article 59, CBA.
[35] The IMF, "Indonesia: Eleventh Review Under the Extended Arrangement – Staff Report; and Press Release on the Executive Board Discussion", January 2004.
[36] Interviews in Indonesia, 14-17 November 2005.
[37] Article 47, CBA.
[38] He was originally sentenced for being allegedly involved in the Bank Bali scandal.
[39] Interviews in Indonesia, 4-6 October 2004.
[40] "Third former BI director convicted", *The Jakarta Post*, 5 April 2003.
[41] Interviews in Indonesia, 4-6 October 2004.